Malayan Cement Industries Sdn Bhd v Golden Island Shipping (L) Bhd

COURT OF APPEAL (PUTRAJAYA) — CIVIL APPEAL NO P-02–2668–11 OF 2012
DAVID WONG, ZAWAWI SALLEH AND PRASAD ABRAHAM JJCA
29 MAY 2017

Contract — Contractual terms — Liquidated damages clause — Respondent agreed to supply 60,000 metric tonnes of iron ore to appellant — Agreement provided that appellant shall place monthly requirement of not less than 4,000 — Agreement contained clause for liquidated damages — Appellant failed to take delivery of 14,311 metric tonnes of iron ore — Whether respondent had burden to prove its loss and as corollary to that, to mitigate its losses — Contracts Act 1950 s 74

Vide an agreement dated 1 April 2004 ('the said agreement'), the respondent had agreed to supply 60,000 metric tonnes of iron ore to the appellant at a price of RM44.50 per metric tonnes and that the appellant shall place a monthly requirement of not less than 4,000 metric tonnes. The said agreement also contained a clause ('cl 13') for liquidated damages. Due to the failure of the appellant to take delivery of the total of 14,311 metric tonnes of iron ore supplied by the respondent, respondent brought a claim against the appellant for a lump of RM636,839.50. At the end of the trial, the learned judicial commissioner ('the JC') allowed the respondent's claim, hence the present appeal. The issue for consideration was whether the respondent had the burden to prove its loss and as a corollary to that, to mitigate its losses where the parties had stipulated liquidated damages in the event of breach in the agreement.

Held, allowing the appeal and setting aside the decision of the learned JC with costs of RM30,000:

(1) The learned JC fell into serious error in holding that in view of cl 13 of the said agreement, the issue of proof of loss and as a corollary to that, to mitigate his losses was a 'non-issue'. Despite the words 'whether or not actual damage or loss is proved to have been caused thereby' contains in s 74 of the Contracts Act 1950, the Malaysian courts have construed the wording in that section to mean that a party would still be under an obligation to prove its loss and to mitigate its losses. In the instant appeal, it was not disputed that the loss was as a result of the shortfall in quality of iron ore which the appellant had agreed to purchase from the respondent. Therefore, the loss could be measured in term of money (see paras 29, 31 & 33).

[Bahasa Malaysia summary

Melalui perjanjian bertarikh 1 April 2004 ('perjanjian tersebut'), responden telah bersetuju untuk membekalkan 60,000 metrik tan bijih besi kepada perayu pada harga RM44.50 setiap metrik tan dan perayu akan memesan keperluan bulanan tidak kurang daripada 4,000 metrik tan. Perjanjian tersebut juga mengandungi klausa ('klausa 13') bagi ganti rugi pembubaran. Akibat kegagalan perayu untuk menerima penyerahan sebanyak 14,311 metrik tan bijih besi yang dibekalkan oleh responden, responden membuat tuntutan terhadap perayu bagi jumlah RM636,839.50. Di akhir perbicaraan, pesuruhjaya kehakiman ('PK') membenarkan tuntutan responden, maka rayuan ini. Isu untuk pertimbangan adalah sama ada responden mempunyai beban untuk membuktikan kerugiannya dan sebagai akibat kepadanya, untuk mengurangkan kerugiannya di mana pihak-pihak telah menetapkan ganti rugi pembubaran sekiranya pelanggaran dalam perjanjian.

Diputuskan, membenarkan rayuan dan mengetepikan keputusan PK yang bijaksana dengan kos sebanyak RM30,000:

(1) PK yang bijaksana telah membuat kesilapan yang serius dalam memutuskan bahawa mengambil kira klausa 13 perjanjian tersebut, isu pembuktian kerugian dan sebagai akibat kepadanya, untuk mengurangkan kerugiannya adalah 'non-issue'. Meskipun perkataan-perkataan 'whether or not actual damage or loss is proved to have been caused thereby' terdapat dalam s 74 Akta Kontrak 1950, mahkamah-mahkamah Malaysia telah mentafsirkan perkataan dalam seksyen tersebut untuk bermaksud bahawa pihak akan masih berada di bawah tanggungjawab untuk membuktikan kerugiannya dan untuk mengurangkan kerugiannya. Dalam rayuan ini, ia tidak dipertikaikan bahawa kerugian tersebut adalah akibat kurangan dalam kualiti bijih besi yang mana perayu telah bersetuju untuk membeli daripada responden. Oleh itu, kerugian boleh diukur dari segi wang (lihat perenggan 29, 31 & 33).]

Notes

For a case on liquidated damages clause, see 3(3) *Mallal's Digest* (5th Ed, 2015) para 4550.

Cases referred to

AMEV-UDC Finance Ltd v Austin (1980) 162 CLR 170, HC (refd)

Dunlop Pneumatic Tyre Co, Ltd v New Garage and Motor Co, Ltd [1914–15] All ER Rep 739; [1915] AC 79, HL (refd)

Hadley and Another v Baxendale and Others [1854] 9 Ex 341 (refd)

Johor Coastal Development Sdn Bhd v Constrajaya Sdn Bhd [2009] 4 MLJ 445; [2009] 4 CLJ 569, FC (refd)

Joo Leong Timber Merchant v Dr Jaswant Singh a/l Jagat Singh [2003] 5 MLJ 116, HC (refd)
Kabatasan Timber Extraction Co v Chong Fah Shing [1969] 2 MLJ 6, FC (refd)
Kok Siak Poo v Perkayuan OKS Sdn Bhd & Ors [1989] 3 MLJ 164, SC (refd)
Malaysian Rubber Development Corp Bhd v Glove Seal Sdn Bhd [1994] 3 MLJ 569, SC (refd)
Maula Bux v Union of India (1969) 2 SCC 554, SC (refd)
Michael C Solle v United Malayan Banking Corporation [1986] 1 MLJ 45; [1984] 1 CLJ 151, FC (refd)
Selva Kumar a/l Murugiah v Thiagarajah a/l Retnasamy [1995] 1 MLJ 817, FC (refd)
WT Malouf Pty Ltd v Brinds Ltd (1981) 52 FLR 442, SC (refd)

Legislation referred to

Contracts Act 1950 ss 74, 75

Appeal from: Civil Appeal No MT4–22–410 of 2005 (High Court, Pulau Pinang)

Michael Chow (CH Cheong with him) (Michael Chai & Co) for the appellant.
Harpal Singh Gill (Harpal Singh & Co) for the respondent.

Zawawi Salleh JCA (delivering judgment of the court):

INTRODUCTION

[1] This appeal turns on a very short and narrow compass, namely, whether the plaintiff ('the appellant') has the burden to prove its loss and as a corollary to that, to mitigate its losses where the parties have stipulated liquidated damages in the event of breach in the agreement.

[2] For convenience, in this judgment, the parties will be referred to as they were in the High Court.

BRIEF FACTUAL BACKGROUND

[3] The relevant factual background giving rise to this appeal may be briefly stated as follows:

(a) the plaintiff is a supplier of iron ore. The defendant is a company which manufactures cement and uses iron ore in its manufacturing process;

(b) vide an agreement dated 1 April 2004 between the plaintiff and the defendant ('the said agreement'), the plaintiff had agreed to supply an approximate total of 60,000 metric tonnes of iron ore to the defendant

A from 1 January–31 December 2004 at a price of RM44.50 per metric tonnes and that the defendant shall place a monthly requirement of not less than 4,000 metric tonnes;

(c) the defendant had in breach of the said agreement failed to take delivery of the total of 14,311 metric tonnes of iron ore supplied by the plaintiff;

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(d) cl 4.2 of the said agreement provides for the price to be fixed at RM44.50 per metre tonnes and cl 13 reads:

> The Company shall and hereby undertakes to purchase from the supplier a minimum quantity of not less than 48,000 mt per annum (ie A minimum of 4,000 mt per month) failing which the Company shall pay the Supplier the shortfall thereof in any event.

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(e) the plaintiff's claim against the defendant is therefore calculated as follows — 14,311 x RM44.50 = RM636,839.50;

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(f) in other words, the plaintiff's claim against the defendant is for a lump of RM636,839.50 being the value of the shortfall of 14,311 metric tonnes of iron ore calculated at the price of RM44.50 per metric tonnes;

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(g) at the end of trial, the learned judicial commissioner ('the learned JC') (as he then was) allowed the amount claimed by plaintiff (RM636,839.50) with interest at the rate of 4%pa from the date of filing of the writ to the date of realisation and costs of RM20,000; and

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(h) being aggrieved with the said decision, the defendant appealed to this court.

FINDINGS OF THE LEARNED JC

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[4] The fulcrum of the learned JC's reasoning in allowing the plaintiff's claim is to be found in the following passages in his grounds of judgment:

> On the contention of the defendant in submission that there was no evidence of loss and mitigation of loss, I find this to be non-issue since parties have agreed and covenanted contractually that the shortfall arising from the inability of the defendant to take up the agreed minimum quantity of the iron ore pursuant to cll 1, 1.1, 4 and 13 shall be the basis of the loss or damage to the plaintiff and pursuant to cl 13 that the defendant has unconditionally agreed that the defendant *shall pay* to the plaintiff *the shortfall thereof in any event*, liquidated damage or loss has been determined by the parties within the said agreement itself. This court must give effect to what the parties have so intended. I do not find merit in this argument.
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> (See additional appeal record at p 16).

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PARTIES COMPETING'S SUBMISSIONS

[5] The focus of criticism which learned counsel for the defendant directs to the decision of the learned JC is that His Lordship was in error in holding that the issue of proving actual loss and failure to mitigate damages were a 'non-issue' since liquidated damages were provided for in cl 13 of the said agreement.

[6] Learned counsel posited that the law is clear that the plaintiff, notwithstanding cl 13 of the said agreement, must still prove its loss and as a corollary to that principle, the plaintiff must mitigate its loss.

[7] Learned counsel further submitted that the general law as to the measure of damages or compensation for a breach of contract is provided under s 74 of the Contracts Act 1950 ('Act 136'). Simply put, the section requires the plaintiff to prove its loss and in the absence of such proof, he would only be entitled to nominal damages. Underpinning the principle is the overriding obligation of party to mitigate their losses.

[8] In support of his submission, reliance was placed on the decision of the Supreme Court in the *Malaysian Rubber Development Corp Bhd v Glove Seal Sdn Bhd* [1994] 3 MLJ 569.

[9] In reply, learned counsel for the plaintiff submitted that the said agreement makes it mandatory for the defendant to purchase from the plaintiff a minimum of 4000 metric tonnes of iron ore per month. It also makes it compulsory for the defendant to compensate the plaintiff for the shortfall thereof in any event should there be a default by the defendant.

[10] It is the contention of learned counsel for the plaintiff that since liquidated damages were provided for in the said agreement, there was no obligation on the part of the plaintiff to prove its loss and as a corollary to that, to mitigate its losses.

[11] Learned counsel further submitted that the terms of the said agreement are very clear in their words and meaning and the court ought to give effect to what the parties have agreed upon (see *Michael C Solle v United Malayan Banking Corporation* [1986] 1 MLJ 45; [1984] 1 CLJ 151 and *Kok Siak Poo v Perkayuan OKS Sdn Bhd & Ors* [1989] 3 MLJ 164).

DISCUSSION AND DECISION

[12] At the outset, it must be recognised that there are a number of advantages to the inclusion of a liquidated damages clause in a contract.

A Among significant advantages are: a liquidated damages clause permits the parties to enter into a contractual relationship with a better understanding of their respective rights and obligations in the event of breach and can eliminate the cost and delay of a complex lost-profits analysis if the relationship breaks down.

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[13] In *AMEV-UDC Finance Ltd v Austin* (1980) 162 CLR 170, Mason and Wilson JJ said at pp 193–194:

> Instead of pursuing a policy of restricting parties to the amount of damages which
> C would be awarded under the general law or developing a new law of compensation for plaintiffs who seek to enforce a penalty clause, the courts should give the parties greater latitude to determine the terms of their contract. In the case of provisions for agreed compensation and, perhaps, provisions limiting liability, that latitude is mutually beneficial to the parties. It makes for greater certainty by allowing the
> D parties to determine more precisely their rights and liabilities consequent upon breach or termination, and thus enables them to provide for compensation in situations where loss may be difficult or impossible to quantify or, if quantifiable, may not be recoverable at common law. And they may do so in a way that avoids costly and time-consuming litigation.

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[14] Construction contracts frequently contain 'liquidated damages' clause in favour of the owner (see for example, cl 40 of PWD Forms 203A (Rev 10/83) and cl 22 of PAM 98). Typically, the clause provides a provision of 'Damages for Non-Completion'. Briefly, the provision indicates that in the
F event of late completion, the contractor shall pay to the employer the LAD specified amount per day of delay until the completion date. The employer may deduct such sum from any monies payable to the contractor under this contract. In addition, the LAD is considered as the actual loss that will be suffered in breach of contract and the contractor agrees to pay the said sum
G without the need of proving damages by the employer.

[15] Statutory provisions for compensation for damages by breach of contract and liquidated damages in Malaysia are found in ss 74 and 75 of Act 136:

H 74 Compensation for loss or damage caused by breach of contract.

(1) When a contract has been broken, the party who suffers by the breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from the breach, or which the parties knew, when they made the contract, to be
I likely to result from the breach of it.

(2) Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

Compensation for failure to discharge obligation resembling those created by contract.

(3) When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default as if the person had contracted to discharge it and had broken his contract.

75 Compensation for breach of contract where penalty stipulated for.

When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for.

[16] Section 74 makes it clear that compensation is not to be given for any remote or indirect loss or damage sustained by reason of the breach. The underlying principle in this section is that a mere breach of contract by a defaulting party would not entitle the other side to claim damages unless the said party has in fact suffered damages because of such breach. Loss and damages which is actually suffered as a result of breach has to be proved and the plaintiff is to be compensated to the extent of actual loss or damage suffered.

[17] Concerning s 75 of Act 136, the Federal Court in *Selva Kumar a/l Murugiah v Thiagarajah a/l Retnasamy* [1995] 1 MLJ 817, held that the employer is required to prove his actual loss suffered in accordance with the general principles of proof of damages. The Federal Court, in interpreting s 75, held that the plaintiff who is claiming for actual damages in an action for breach of contract must still prove the actual damages or reasonable compensation in accordance with the settled principles in the English landmark case of *Hadley and Another v Baxendale and Others* [1854] 9 Ex 341. Any failure to prove such damages will result in the refusal of the court to award such damages. Section 75 of Act 136 provides an instance in which Malaysian law departs significantly from the line of English common law.

[18] Under common law, a liquidated damages clause must comply with the 'penalty' principle establish by Lord Dunedin in the landmark case of *Dunlop Pneumatic Tyre Co, Ltd v New Garage and Motor Co, Ltd* [1914–15] All ER Rep 739; [1915] AC 79, that:

The essence of liquidated damages is a genuine covenanted pre-estimate of loss.

[19] What is meant by the term 'genuine pre-estimate' was further explained in *WT Malouf Pty Ltd v Brinds Ltd* (1981) 52 FLR 442 as:

A genuine pre-estimate means a pre-estimate which is objectively of that character: that is to say, a figure which may properly be called so in the light of the contract and the inherent circumstances. It will not be enough merely that the parties honestly believed it to be so.

[20] The courts in Malaysia have concluded that the distinction between liquidated damages and penalties does not apply, the situation being governed by s 75 of Act 136 which has been held to have erased this distinction.

[21] In addition, there is a general duty requiring that reasonable steps to be taken to mitigate losses flowing a breach particularly in the case of anticipatory breach. The party who has failed to mitigate the losses cannot later recover any such loss flowing from his neglect. This is a long established principle applied in *Kabatasan Timber Extraction Co v Chong Fah Shing* [1969] 2 MLJ 6. The Federal Court held that it was the duty of the respondent to take reasonable steps to mitigate the damages caused by the appellant when he failed to deliver logs to the mill but left them some 500 ft away. This principle also applied in *Joo Leong Timber Merchant v Dr Jaswant Singh a/l Jagat Singh* [2003] 5 MLJ 116. The respondent counterclaimed for loss of rental income against appellant's claim for the balance sum due for the completed building works was dismissed by the High Court due to respondent's failure to show that he had taken all reasonable steps to mitigate his damage.

[22] In *Johor Coastal Development Sdn Bhd v Constrajaya Sdn Bhd* [2009] 4 MLJ 445; [2009] 4 CLJ 569, the Federal Court was asked to review its earlier decision in the case of *Selva Kumar a/l Murugiah*. The appellant obtained leave to the Federal Court on the following two questions:

(a) Whether that part of the decision in *Selva Kumar a/l Murugiah v Thiagarajah a/l Retnasamy* [1995] 1 MLJ 817 which obliges a party having the benefit of a liquidated damages clause to prove its losses, notwithstanding the words in Contracts Act 1950 'whether or not actual damage or loss is proved to have been caused thereby', is correct; and

(b) Whether or not parties entering into a contract are entitled to contract out of the provisions of Contracts Act 1950.

[23] The Federal Court dismissed the appeal by a majority of 2–1. The majority (per Arifin Zakaria CJ (Malaya) (as he then was) and Alaudin Sheriff PCA concurring) reaffirmed the principles set out by the Federal Court in *Selva Kumar a/l Murugiah*, namely:

(a) the words in s 75 of Act 136 'whether or not actual damage or loss is proved to have been caused thereby' must be given a restricted construction. Thus, a party who is claiming for damages in an action for breach of contract must still produce evidence to prove the actual loss or the reasonable compensation. Any failure to prove such loss will result in the refusal of the court to award such damages; and

(b) however, for cases where the court finds it difficult to assess damages for the actual damage as there is no known measure of damages employable, and yet the evidence clearly shows some real loss inherently which is not

too remote, the stipulated sum may be recoverable. The court ought to award substantial damages as opposed to nominal damages which are reasonable and fair according to the court's good sense and fair play. In any event, the damages awarded must not exceed the sum so named in the contractual provision.

[24] Based on the foregoing reasons, the majority answered the first question in the affirmative. The majority did not answer the second question as they opined that there was no clear provision in the agreements which excluded the application of s 75 of Act 136.

[25] The minority (per Hashim Yusof FCJ (dissenting)) held as follows:

(a) the monies were rightly forfeited by the appellant, being an amount that was reasonable in view of the nature of the project and its abandonment by the respondent three years after the agreements were signed. Although proof of loss and damages could be given, it would be a very lengthy process. It was to avoid this lengthy process that the parties agreed on a stipulated sum in the event of a breach. It could not be the case that the innocent party would be the one to have to prove the loss; and

(b) the parties had expressly agreed and named the sums payable in case of breach as reasonable compensation to the non-defaulting party. The parties further waived any objection thereafter that those sums would be otherwise than fair or reasonable compensation. Such stipulation was not contrary to s 75 of Act 136.

[26] As such, the appellant was entitled to receive from the respondent reasonable compensation not exceeding the sum so named in the agreements, whether or not actual damage or loss is proved to have been caused thereby. Thus, the minority answered the first question in the negative and the second question, positive.

[27] As the law stands now, for a claim of liquidated damages under s 75 of the Act 136, the words 'whether or not actual damage or loss is proved to have been caused thereby' cannot be relied upon to dispense with proof. The plaintiff is totally not entitled to recover his loss if he failed in taking the duty of mitigation.

[28] With these principles in the forefront of our minds, we now proceed to consider the issue posed for our consideration.

[29] With respect, we are of the opinion that the learned JC fell into serious error in holding that in view of cl 13 of the said agreement, the issue of proof

of loss and as a corollary to that, to mitigate his losses was a 'non-issue'. As we have alluded to earlier, despite the words 'whether or not actual damage or loss is proved to have been caused thereby' contains in s 74, the Malaysian courts have construed the wording in that section to mean that a party would still be under an obligation to prove its loss and to mitigate its losses.

[30] We also would like to refer the case of *Maula Bux v Union of India* (1969) 2 SCC 554. In this case, a division bench of the Delhi High Court had upheld the finding of a single judge who had set aside the arbitral award on the ground that the liquidated damages had been made even though no evidence had been led to prove any loss or damages. The court stated:

> It is true that in every case of breach of contract the person aggrieved by the breach is not required to prove actual loss or damage suffered by him before he can claim a decree, and the court is competent to award reasonable compensation in case of breach even if no actual damage is proved to have been suffered in consequence of the breach of contract. But the expression 'whether or not actual damage or loss is proved to have been caused thereby' is intended to cover different classes of contracts which come before the courts. In case of breach of some contracts it may be impossible for the court to assess compensation arising from breach, while in other cases compensation can be calculated in accordance with established rules. Where the court is unable to assess the compensation, the sum named by the parties if it be regarded as a genuine pre-estimate may be taken into consideration as the measure of reasonable compensation, but not if the sum named is in the nature of a penalty. Where loss in terms of money can be determined, the party claiming compensation must prove the loss suffered by him.

[31] In this instant appeal, it is not disputed that the loss is as a result of the shortfall in quality of iron ore which the defendant had agreed to purchase from the plaintiff. Therefore, the loss can be measured in term of money. In fact, the learned JC had allowed the plaintiff's claim in sum of RM636,839.50.

[32] In this instant appeal, PW1 in his witness statement had boldly proclaimed that the plaintiff was not obliged to mitigate its loss. This bold statement goes against the judgment of the Court of Appeal given on 1 March 2011 when allowing the defendant's appeal against the decision of the High Court in entering summary judgment against the defendant in favour of the plaintiff. That judgment identified two issues for trial:

(a) whether the plaintiff had breached the said agreement; and

(b) whether the plaintiff had mitigated its losses.

[33] The evidence on record also shows that the plaintiff was a middle man sourcing supplies from third parties. The law is clear that the plaintiff, notwithstanding cl 13 of the said agreement, must still prove its loss and as a corollary to that principle, the plaintiff must mitigate its losses.

CONCLUSION

[34] For the foregoing reasons, we must answer the question posed in the affirmative. Consequently, we allow the appeal and set aside the decision of the learned JC with costs of RM30,000. So ordered.

Appeal allowed; decision of the learned JC set aside with costs of RM30,000.

Reported by Dzulqarnain Ab Fatar